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The Honorable Marc Barreca
United States Bankruptcy Judge
Hearing Date: September 26, 2018
Hearing Time: 10:00 AM
Hearing Location:

Marysville Municipal Court
1015 State Ave. Courtroom 1
Marysville, WA 98270

6 UNITED STATES BANKRUPTCY COURT
7 WESTERN DISTRICT OF WASHINGTON AT SEATTLE

8 In Re:

9 Brian Lettman,

10 Debtor.

Case No. 17-10063-MLB

In Proceedings under Chapter 7

11 **REPLY TO CREDITOR'S RESPONSE**
12 **TO MOTION FOR SANCTIONS FOR**
13 **VIOLATION OF AUTOMATIC STAY**

14
15 **REPLY**

16 **1. Sound Mind LLC ceased to be a legal entity on March 13, 2016 because its'**
17 **organization and termination is governed by Delaware law.** In Washington, a foreign
18 limited liability company ("FLLC") "registered *to do business in this state* is subject to
19 RCW 23.95.500 relating to the effect of registration and the governing law..." (RCW
20 25.15.316, emphasis added). RCW 23.95.500(1) states "[t]his chapter does not authorize
21 this state to *regulate the organization or internal affairs* of a foreign entity registered to do
22 business in this state, *or govern the liability that a person has as an interest holder or*
governor for a debt, obligation, or other liability of the foreign entity. (Emphasis added).

DEBTOR'S REPLY- 1

1 Under Delaware law, a Certificate of Formation must be filed to form a limited liability
2 company (LLC). 6 Del. C. § 18-201(a). A Delaware LLC “shall cease to be a legal entity
3 upon cancellation of its’ Certificate of Formation. *Id*; See also *Chantz Enterprises, LLC v.*
4 *JHL Brighton Desing/Décor Center, LLC*, Del. Super., C.A. No. 09C-06-072, MJB (June
5 30, 2010). Statutory authority is required in Delaware to prolong the life of a legal entity
6 beyond the date it was terminated. *In re Citadel Indus., Inc.*, 423 A.2d 500, 503 (Del.Ch.
7 1980).

8 Sound Mind LLC was a Delaware entity. Its Certificate of Formation was filed in
9 Delaware pursuant to 6 Del. C. § 18-201(a), and eventually cancelled by operation of law
10 under 6 Del. C. § 18-104(d). Sound Mind LLC ceased to be a legal entity on March 13,
11 2016 unless Creditor can provide statutory authority under the Delaware Code extending
12 the life of Sound Mind LLC beyond the date its Certificate of Formation was canceled. See
13 *Chantz Enterprises, LLC v. JHL Brighton Desing/Décor Center, LLC*, Del. Super., C.A.
14 No. 09C-06-072, MJB (June 30, 2010); See also *In re Citadel Indus, Inc.* at 503.

15 Creditor seems to argue in its Response that a party need only admit in court
16 pleadings that a legal entity exists. This is a misstatement, or at a minimum a
17 misunderstanding of law. Creditor’s Response, Attachment A, demonstrates that both
18 Washington and Delaware have specific requirements for a legal entity to be organized.
19 Debtor’s admissions in state court proceeding that Sound Mind LLC is a Washington LLC
20 as stated in the Creditor’s complaint does not make it so under Washington or Delaware
21 Law. Neither do communications from the Debtor, his previous counsel, or any other party.
22 If that were true, a debtor and creditor only need contrive a legal entity into existence to
protect a debtor’s assets from the bankruptcy estate. While this matter is complicated, the

DEBTOR’S REPLY- 2

1 fact remains that Sound Mind LLC did not exist as a legal entity under Delaware law at the
2 time Debtor filed his bankruptcy.

3 **2. Sound Mind LLC was not revived under 6 Del. C. § 18-1108 because it does**
4 **not apply.** When a Certificate of Formation is cancelled for failure to pay the annual tax
5 due under 6 Del. C. § 18-1107, the cancellation becomes effective three years after the due
6 date. 6 Del.C. § 18-1108. If the taxes are paid within the three-year tolling period, the
7 Certificate of Formation is revived. *Id.*; *Chantz Enterprises, LLC v. JHL Brighton*
8 *Desing/Décor Center, LLC*, Del. Super., C.A. No. 09C-06-072, MJB (June 30, 2010).
9 Cancellation of the Certificate of Formation for failure to provide a registered agent is
10 treated differently than other methods of cancellation and does not have any such revival
11 period. See *Steven B. Trusa v. Norman Nepo, et al*, Del. Ch., C.A. No, 12071-VCMR,
12 Montgomery Reeves, (April 13, 2017).

13 Sound Mind LLC's Certificate of Formation was canceled by operation of law for
14 failing to provide a registered agent, not for failure to pay annual taxes under § 18-1107.
15 Although Creditor argues that Sound Mind LLC was somehow revived under 6 Del. C. §
16 18-1108, this section of the code only applies to entities cancelled for failure to pay annual
17 taxes, which is not what happened in this case.

18 **3. Sound Mind LLC was not revived by the Washington Foreign Registration**
19 **Statement.** As mentioned above, the organization of a foreign entity is governed by the
20 state in which it was organized, not by RCW 23.95.500. Debtor has not revived Sound
21 Mind LLC with the State of Delaware after the Certificate of Formation was cancelled. In
22 support of its' assertion that Sound Mind LLC was revived, Creditor provided a
Washington Foreign Registration Statement for Sound Mind LLC filed on October 27,

DEBTOR'S REPLY- 3

1 2017 and a Certificate of Good Standing from Delaware that did not convert properly to
2 PDF. See Exhibit 13 of the Declaration of Klaus O Snyder.

3 Assuming creditor could have properly examined the certificate, it would have
4 realized that the Sound Mind LLC identified in Exhibit 13 is a separate legal entity
5 incorporated in Delaware on October 26, 2017 under file number 6593411 (“Sound Mind
6 2”). The Sound Mind LLC canceled March 13, 2016, that is at issue in this case, was
7 incorporated in Delaware on November 13, 2012 under file number 5240954 (“Sound
8 Mind 1”). Although the State of Washington has recognized both Sound Mind LLC’s as
9 foreign entities under the same UBI number, each entity is legally separate under Delaware
10 law. While Sound Mind 2 is in good standing in Delaware, Sound Mind 1’s Certificate of
11 Formation was canceled and has never been revived.

12 4. **A Special Warranty Deed conveying property to Sound Mind LLC, a**
13 **Delaware Limited Liability Company has no legal affect on the organization or**
14 **termination of an entity.** As stated above, Washington and Delaware have specific
15 requirements for a legal entity to be organized. Both state also have specific processes to
16 terminate an entity. Debtor is unaware of any statute in either state, and Creditor has not
17 provided one, that indicates an entity remains in existence simply because there is a deed
18 conveying real property to a party identified as a Limited Liability Company.

19 Creditor provides a Special Warranty Deed showing real property conveyed to Sound
20 Mind LLC, a Delaware Limited Liability Company on March 5, 2014. See Declaration of
21 Klaus Snyder Exhibit 15. Beside providing evidence that Creditor should have know at the
22 time it filed its complaint in state court that Sound Mind LLC was incorporated in
Delaware, the deed does not circumvent the cancellation of Sound Mind LLC’s Certificate

DEBTOR’S REPLY- 4

1 of Formation in Delaware. Real property cannot be owned by a separate entity that does
2 not legally exist. As a result, the real property is effectively transferred to the debtor
3 personally as a sole proprietor thus becoming property of the bankruptcy estate.

4 **3. Creditor's request for sanctions and attorney fees is improper.** Sanctions
5 under Rule 9011 are improper when a party's argument is nonfrivolous, and supported by
6 law and evidence. Any such sanctions may only be granted by a separate motion after
7 giving notice and an opportunity to respond. FRBP Rule 9011(c).

8 In this case, Creditor's request is not by separate motion after giving proper notice.
9 However, Creditor makes two assertions in support of its request for sanctions. First,
10 Creditor asserts "Debtor misrepresents Delaware law" to this Court. Unlike Creditor's
11 response, Debtor's pleadings are supported by statutory law and case law applying such
12 statutory laws. Yet, Creditor's attorney admits he did not take the time to research
13 Delaware Law. (ECF No. 46, Paragraph IV.A) Instead, he simply provides this Court with
14 several Delaware and Washington statutes with his personal interpretation. Although
15 Creditor may not agree with Debtor's arguments, disagreement is not enough to merit
16 sanctions and attorney fees.

17 Second, Creditor asserts Debtor has used multiple attorneys to "put the squeeze" on
18 Brown Electric and its attorney. While Debtor has employed other attorneys, neither of his
19 prior attorneys fully researched the matter, or had a full understanding of the law. In fact,
20 the issues in controversy were never litigated. As shown in the exhibits provided by
21 Creditor, any time it came close to being litigated Creditor's attorney threatened a motion
22 for Rule 9011 Sanctions. Base on this pattern, it appears Creditor's attorney was the party

1 who "put the squeeze" on Debtor and his attorneys to prevent this issue from every being
2 resolved. Thus, Creditors request for sanctions and attorney fees should be denied.

3 DATED: This 21st day of September 2018.

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5 By: /s/ Brad L. Puffpaff
6 Brad L Puffpaff, WSBA #46434
7 Attorney for Debtor
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DEBTOR'S REPLY- 6